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FEBRUARY 10, 1986

CHEMICAL & ENGINEERING

NEWS

Chemical industry gears up for U.S.-Canada free trade talks
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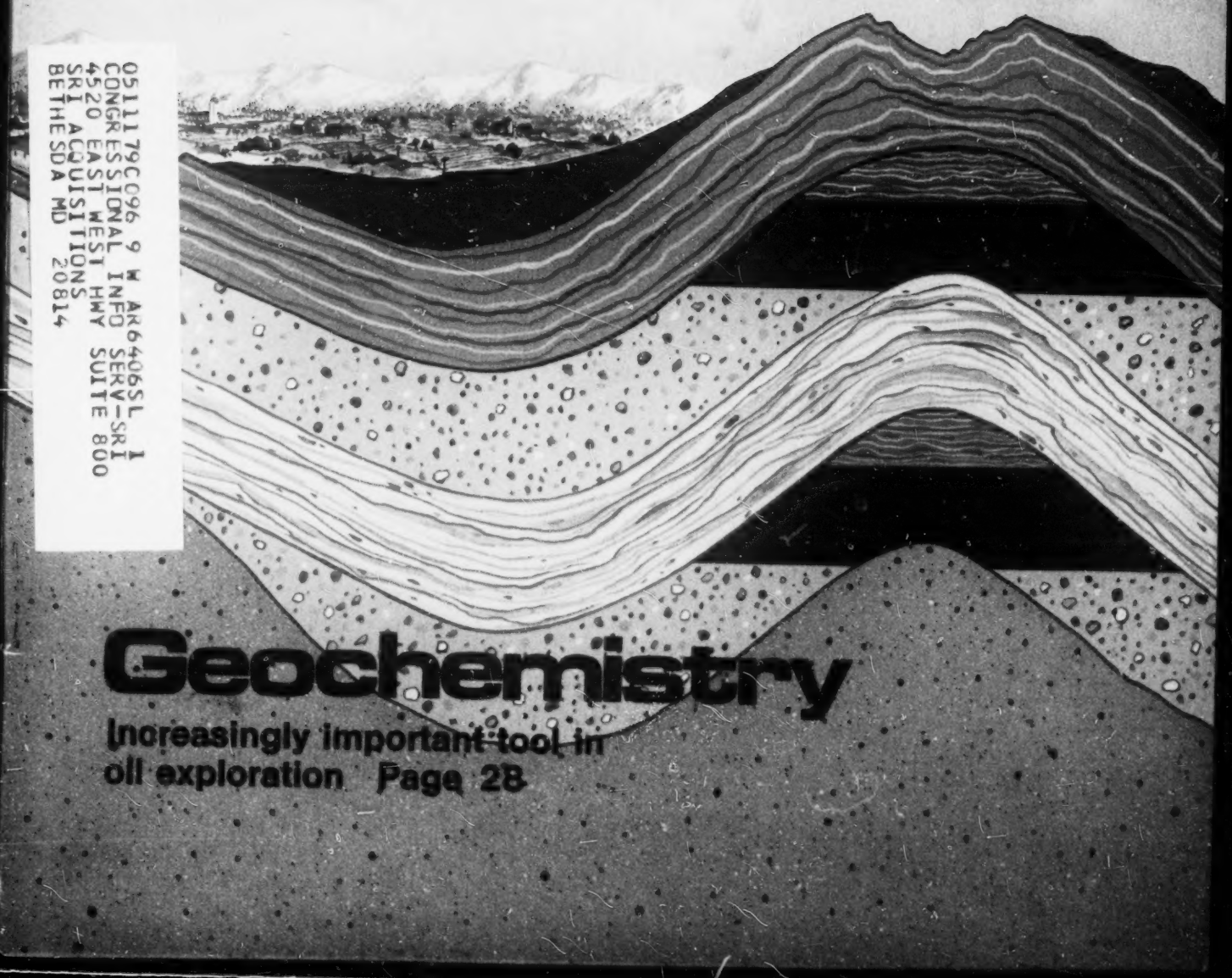

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Increasingly important tool in oil exploration Page 28

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NEWS

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Chemical Industry Not Enthusiastic Over U.S.-Canada Free Trade Talks

U.S. industry leaders seem more concerned about what they may lose, seeing only additional competition and little or no market gains

Earl V. Anderson, C&EN New York

In an earlier article (Sept. 23, 1985, page 7) C&EN indicated that Canadian Prime Minister Brian Mulroney would soon approach the U.S. with a proposal for negotiations aimed at freeing trade between the two countries. It also analyzed the Canadian chemical industry's attitude toward freer trade with the U.S.

Three days after that article appeared, Mulroney did, in fact, phone President Reagan suggesting that Canada and the U.S. explore the scope of and prospects for a new trade agreement. Mulroney wanted to aim for the "broadest possible package of mutually beneficial reductions in barriers to trade in goods and services."

As expected, President Reagan welcomed Mulroney's proposal. On Dec. 10, as required by law, he formally notified Congress that he intended to enter into negotiations on a bilateral free trade arrangement with Canada. It's very likely that these negotiations will start soon—probably this spring.

With its strong interest in international trade, the U.S. chemical industry naturally has been following the U.S.-Canada free trade developments closely. This article takes a look at how the industry feels about them.

In 1911, Canada and the U.S. negotiated the Reciprocity Agreement, which would have reduced tariffs substantially in both countries. But before the agreement could be ratified in either country, a Canadian election intervened. The rallying cry in Canada was, "No truck nor trade with the Yankees." And the ruling Liberal government at the time was resoundingly voted out of office for its attempt at freeing trade with the U.S.

Now, 75 years later, the Canadians have initiated the idea of free or freer trade between the two countries. Again, it is a hot political and economic topic, both north and south of the border. Within the U.S. chemical industry, no one is running around crying, "No truck nor trade with the Canadians." But there is no visible groundswell of support for the concept coming out of the industry either.

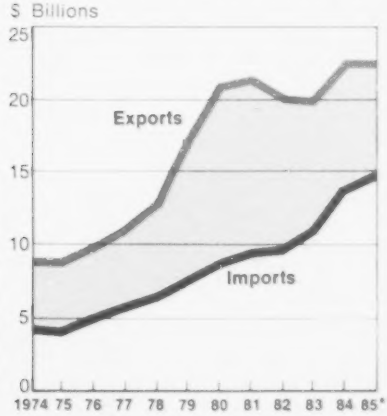
To be sure, a few embrace the principle of unvarnished free trade, no matter what its shape or form. And because Canada is the U.S.'s largest trading partner, those people think it only reasonable that the two should get together at the bargaining table. In the chemical industry, however, they are the minority.

At the other extreme, some people emphatically oppose any attempt to negotiate an agreement that would make it easier for Canadian chemicals to move into U.S. markets. They are not looking at principles; they are looking at products. And when they compare the size of the Canadian market with the U.S. market, which is 10 times larger, they wonder how a free trade agreement could possibly benefit them.

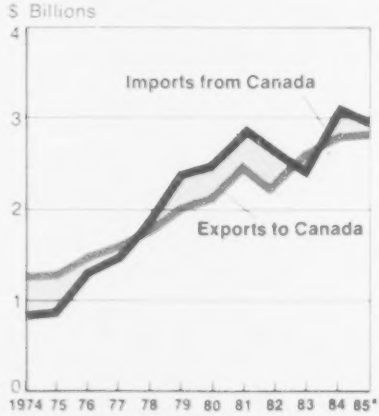
Attitudes such as these are the extremes, but it's not difficult to find a few of them scattered throughout the U.S. chemical industry. Neither one, however, can be construed as representing the industry's position on the pending trade talks.

In the strict sense of the word, the industry has no position. In general, it is less than enthusiastic about the pending U.S.-Canada free trade talks. Another generality: Basic, commodity petrochemical producers tend to be less enthusiastic (or more opposed) to the idea of U.S.-Canadian free trade than producers of downstream products. Not surpris-

U.S. clings to shrinking chemical trade surplus . . .



. . . but chemical trade with Canada is in the red



a C&EN estimate. **Source:** U.S. Bureau of the Census

Canada is a major U.S. supplier for fertilizer, inorganics, and radioactive materials

$ Millions	U.S. chemical exports			U.S. chemical imports			Trade balance	
	World	Canada	% Canada	World	Canada	% Canada	World	Canada
Organic chemicals	$ 6,050	$ 662	10.9%	$ 4,604	$ 576	12.5%	$1446	$ 86
Inorganic chemicals	2,172	302	13.9	1,983	720	36.3	189	−418
Radioactive & associated materials	1,263	17	1.4	1,346	420	31.2	−83	−403
Dyeing, tanning, & coloring materials	133	34	25.6	347	3	0.9	−214	31
Pigments, paints & varnishes	332	112	33.7	246	30	12.2	86	82
Medicinals & pharmaceuticals	2,814	196	7.0	1,057	42	4.0	1757	154
Flavors, perfumes, cosmetics & toiletries	488	64	13.1	550	21	3.8	−62	43
Cleaning & polishing materials	310	50	16.1	159	45	28.3	151	5
Fertilizers, manufactured	2,105	182	8.7	1,013	711	70.2	1092	−529
Explosives & pyrotechnics	111	25	22.5	116	30	25.9	−5	−5
Plastics & resins	3,834	700	18.3	1,636	330	20.2	2198	370
Pesticides & disinfectants	643	137	21.3	434	15	3.5	209	122
Miscellaneous chemical products	1,905	319	16.8	984	57	5.6	921	262
TOTAL	$22,160	$2800	12.6%	$14,475	$3000	20.7%	$7685	$−200

Source: C&EN estimates based on 10-month data

ingly, that's the exact opposite of the feelings permeating the Canadian chemical industry. There, the basic petrochemical producers ardently push free trade with the U.S. The opposition comes from the downstream producers.

To varying degrees, basic chemicals producers in the U.S. see only additional competition and little or no new market opportunities. Some downstream producers see less-expensive raw materials and the possibility of additional markets.

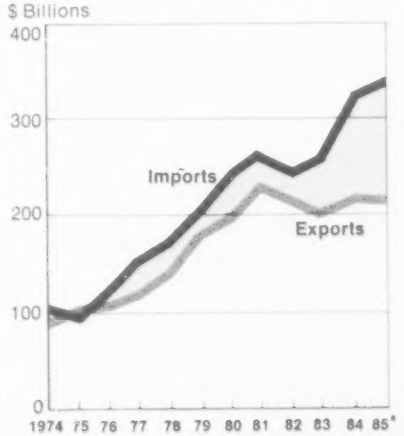
But the generalities end there. When specific products are mentioned, companies tend to have a more specific attitude. Producers of polyethylene and styrene, for instance, do not want to see tariffs on those products eliminated for Canadian imports. According to one trade expert who knows well the pulse of the chemical industry on trade matters, Canada-U.S. free trade has been, until now, almost a nonissue for the chemical industry. No leading industry spokesman has come out and flatly denounced it. That's just not the statesmanlike thing to do. On the other hand, nobody has gone resolutely to bat for it either.

Now, however, U.S.-Canada free trade looms as a significant issue for the chemical industry. With the negotiations likely to begin around May, the industry trade experts who interface with official Washington are gearing up to protect their industry's flanks. Until recently, the chemical industry's major input into the government's preparation for trade negotiations with Canada has been a set of principles compiled last year by the Chemical Manufacturers Association. Those principles do not concern specific chemical products, or chemical industry sectors. Instead, they are issues that CMA believes the U.S. government should address before entering into any bilateral free trade agreement with Canada.

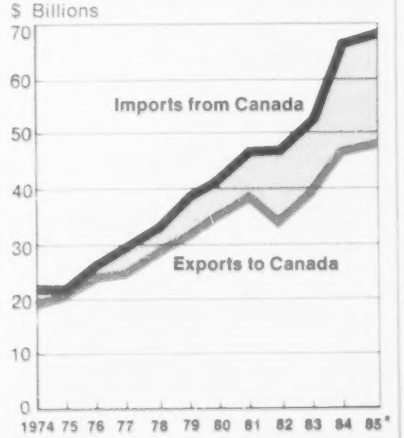
Just last week, however, the Industry Sector Advisory Committee for Chemicals (ISAC-3) sent to U.S. Trade Representative (USTR) Clayton Yeutter a "refined" set of principles based on CMA's earlier work. ISAC-3 is one of many ISACs formed during the Tokyo round of multilateral trade negotiations, which ended in 1979, to funnel industry information and opinion into the trade representative's office.

ISAC business is confidential, but indications are that ISAC-3's refined principles don't stray too far from the framework provided by CMA. One major difference: Although the new ISAC principles focus particularly on the U.S.-Canadian trade

U.S. trade deficit continues to mount . . .



. . . and so does U.S. trade deficit with Canada



* C&EN estimate Source: U.S. Bureau of the Census

talks, they can be adopted for bilateral negotiations with almost any nation.

Some of CMA's principles are pretty straightforward. CMA believes, for instance, that a bilateral free trade agreement with Canada should confer balanced benefits to both countries. One country should not end up with a better deal to the detriment of the other.

Almost everyone acquainted with U.S. and Canadian trade anticipates that the bilateral trade talks will include a healthy dose of tariff cutting. In fact, negotiators may attempt to eliminate tariffs completely on trade between the two countries.

Most of that trade already is duty free. Those tariffs that remain are mostly on manufactured products. On average, Canadian duties are higher than those in the U.S. tariff schedule. However, CMA doesn't think the negotiations should become only an exercise in tariff cutting. They also should address nontariff barriers to trade. One in particular is Canadian energy pricing policies that give that country's petrochemical producers a preferential feedstock price advantage. Another is Canadian restrictions on foreign investment.

Both issues are less onerous than they were even a year ago. The U.S. chemical industry's concern about Canada's internal energy policies was shaped in the early 1980s when the Liberal government of then-Prime Minister Pierre Trudeau launched its National Energy Policy. At the time, right after the second oil crisis, world prices for crude oil were skyrocketing.

Canada's National Energy Policy was designed, among other things, to keep Canadian oil and natural gas prices below world or U.S. prices to protect Canadian consumers. It was molded to "Canadianize" the oil industry. And its tax and royalty provisions raised vast amounts of revenue for the federal government and the energy-producing provinces.

That policy also meant that Canadian petrochemical producers would have a distinct advantage in feedstock costs over their U.S. competitors. They enjoyed that advantage for only a short time, however. Pricing policies were based on the assumption that world oil prices would move steadily upward. When those prices later started dropping instead, the Canadian petrochemical feedstock advantage disappeared.

A little more than a year ago, Mulroney's Conservatives replaced Trudeau's Liberals in Ottawa. Since then, the National Energy Policy has been replaced by energy policies designed to bring flexible, market-oriented pricing back into Canadian oil and natural gas.

CMA recognizes, of course, that Canadian energy pricing policies have improved considerably in the past year. It also recognizes, however, that in government nothing is forever. Thus, CMA is cautioning the U.S. Trade Representative to make sure that present and future Canadian policies relating to petrochemical feedstock supply and price do not serve as a barrier to otherwise fair competition.

That same cautious attitude has been directed toward Canadian policies on foreign investment. During the Trudeau Administration, "FIRA" was a buzzword in foreign investment circles. FIRA stood for Foreign Investment Review Act. It also epitomized restrictive foreign investment policies.

One of the major objections to FIRA was that, to win approval for an investment in Canada, a foreign company had to agree to certain "performance" requirements, such as domestic sourcing for raw materials. Strictly Canadian companies did not have to meet those requirements.

Because of this, the U.S. submitted a complaint against FIRA to the General Agreement on Tariffs & Trade (GATT), the international body that sets the trade rules for most of the world's major trading nations. In 1983, GATT ruled that FIRA did, indeed, violate GATT Article III.

Just as it did with Canadian energy policies, the Mulroney government started changing foreign investment policies after it came into office. FIRA has been replaced by a much less restrictive Investment Canada Act.

However, in CMA's view, the new investment act is not lily white. Although the new legislation makes foreign investment in Canada much more welcome than FIRA did, some restrictions do remain, especially on foreign acquisitions of existing Canadian companies.

So, just as it did with Canadian energy policies, CMA feels it remains to be seen how the new legislation is implemented. Meanwhile, it wants U.S. negotiators to get rid of discriminatory Canadian investment restrictions (other than those dealing with national security) before they reach any tariff-cutting agreement.

Although energy-feedstock pricing policies and foreign investment restrictions head the chemical industry's list of important nontariff barriers, they are not the only ones. As actual trade negotiations draw closer, intellectual property rights figure to become a more important issue. In fact, intellectual property rights have become a hot international economic issue on a scale much broader than just U.S.-Canadian trade. U.S. companies, including many in the chemical and pharmaceutical industries, are annoyed because they are not receiving adequate protection for their intellectual property, such as patents and copyrights, in some countries. Without that protection, the companies claim they are losing the battle for international markets to unfair competition.

Congress has taken heed. It has written provisions aimed at encouraging such protection abroad into the Trade & Tariff Act of 1984. Intellectual property rights have been included in several previous bilateral trade and investment negotiations. In fact, some industry groups are pushing to have them included in the proposed multilateral trade negotiations.

CMA wants intellectual property right protection included as part of any free trade negotiations with Canada. Although Canada is far from the worst offender, there are some problem areas, particularly in pharmaceuticals.

For some time, in fact, major U.S. drug companies have been fighting against what they see as inadequate pharmaceutical patent protection in

U.S.-Canadian chemical trade

A much larger share of the total for Canada . . .

1985 Canadian chemical exports = $4.17 billion

1985 Canadian chemical imports = $4.04 billion

. . . than it is for the U.S.

1985 U.S. chemical exports = $22.16 billion

1985 U.S. chemical imports = $14.48 billion

Note: 1985 figures are C&EN estimates based on 10-month data from U.S. Bureau of the Census, Statistics Canada

Canada. They are peeved at old Canadian laws that allow generic drug companies to move swiftly in copying new drugs developed by multinational companies.

The Mulroney government is supposed to start reconsidering the pharmaceutical patent protection issue this year. Experts in the U.S., however, aren't optimistic about getting all of the changes they think are necessary. For instance, multinational drug companies—not just those based in the U.S.—want 17 years of basic patent protection. Informed betting is that the Mulroney government is considering eight years. That's much better than what exists today (virtually none), but it's far short of the multinationals' demands.

Canadian generic drug producers naturally are resisting any changes in the existing law. So are the provinces of Ontario and Quebec, which depend on less-expensive generic substitutes in their drug programs for the poor and elderly.

In the U.S., however, major U.S. drug companies argue that they are being robbed of years of research and development costs, not to mention lost profits. By now, officials at the trade representative's office have been made well aware that intellectual property rights is a contentious issue. There's little doubt that it will be on the agenda when the U.S.-Canadian trade talks begin.

Despite the importance of those and other nontariff barriers, tariff cutting will be the major chemical industry concern in the U.S.-Canada trade negotiations, just as it has been in virtually all past trade negotiations. It's possible that existing tariffs on chemical trade between the two countries will be eliminated completely during the negotiations. If that should happen, the chemical industry wants it to happen on as broad a base as possible.

This is a key issue for the chemical industry. If tariffs are to be eliminated completely, CMA wants it to be across the board—that is, it should include all chemicals and related products and not be limited to chemical industry subsectors or specific products. For the U.S. chemical industry, it is a logical position to take. Canada has tried several times to convince the U.S. to grant duty-free treatment to selected Canadian petrochemicals. The first attempt originated out of Alberta right after the Tokyo round ended in 1979.

At the time, energy-rich Alberta was starting to develop its world-scale petrochemical industry. The U.S. was scratching for oil and natural gas supplies. Alberta offered to supply the U.S. with natural gas in return for zero tariffs on several petrochemicals that the province was producing or planned to produce.

The Albertans took their proposal to Congress, but it never got off the ground. Later, when free trade negotiations between the two countries became a more serious topic, "sectoral" free trade was suggested as the approach with the best chance of success. After all, the U.S. and Canada already had a successful, 20-year trade agreement covering automobiles and parts.

One of the sectoral candidates proposed by the Canadians was again petrochemicals. Before this sectoral approach advanced very far, government reins changed hands in Ottawa. When the Mulroney government picked up the issue of free trade with the U.S., it adopted the broad-based approach.

CMA favors such an approach for chemicals because it believes it is the only way that negotiators will be able to achieve reciprocity—or balanced benefits—in chemicals. Very few disagree that a free trade pact limited only to basic petrochemicals would benefit Canadian producers and hurt U.S. producers.

That could become a tough issue for negotiators to tackle. CMA's counterpart in Canada, the Canadi-

an Chemical Producers Association, strongly supports free trade in petrochemicals. But CCPA is much less enthusiastic about duty-free trade in downstream products. Many of its smaller member companies believe they could be hurt badly if their domestic markets were opened to duty-free imports from the U.S.

CMA, meanwhile, believes its members could be hurt by one other aspect of a free trade arrangement between the U.S. and Canada. It is concerned that products from a third country that are dutiable in the U.S. could slip into the country duty free by way of Canada.

It's an old ploy. Producers in third countries could ship their products to Canada, where they would go through minor formulating or finishing operations. Then, by shipping them to the U.S. out of Canada, these products would sidestep U.S. tariffs.

To prevent this from happening, CMA wants a minimum level of "Canadian value added" established as a condition for duty-free entry into the U.S. The value-added threshold, says CMA, should be high enough to prevent these unfair transshipments. CMA suggests a level of 70%. That's twice as high as the 35% value-added requirements set by the Generalized System of Preferences (GSP), which grants duty-free treatment to products of eligible developing countries. The Caribbean Basin Initiative, designed to give preferential tariff treatment to products from Caribbean countries, also has a 35% value-added provision.

But, as CMA points out, Canada is not a developing country. It should not be given the liberal domestic value-added requirements that developing countries are receiving under GSP and Caribbean Basin Initiative.

CMA suggests, however, that the value of raw materials or components shipped from the U.S. to Canada be considered "Canadian value added" in determining whether a Canadian product meets the 70% test. That, CMA says, will help to promote bilateral trade.

CMA has some other caveats about duty-free treatment of Canadian chemical imports. It believes that any free trade agreement should contain a "snap-back" provision, which automatically would return tariffs to their normal rates if any conditions of the agreement no longer are fulfilled. If, for instance, Canada reimposed investment restrictions or reverted back to unfair energy pricing policies, then duties of chemical imports from Canada would snap back to their normal rates.

Intent on protecting the industry's flanks, CMA has brought several other issues to the attention of the U.S. Trade Representative. It wants surcharges imposed to correct temporary distortions of trade caused, for instance, by currency fluctuations.

CMA also assumes that U.S. unfair trade statutes will continue to apply to imports from Canada. In other words, Canada's exports to the U.S. will continue to be subject to antidumping and countervailing duty laws designed to protect U.S. industries injured by unfair import competition.

That may be more hope than assumption on CMA's part. A major reason that Canada started the ball rolling toward free trade talks with the U.S. was its fear of growing U.S. protectionism. It hopes to insulate its exports to the U.S. from further protectionist action by getting special treatment for them, including possible exemption from the U.S. unfair trade practices statutes.

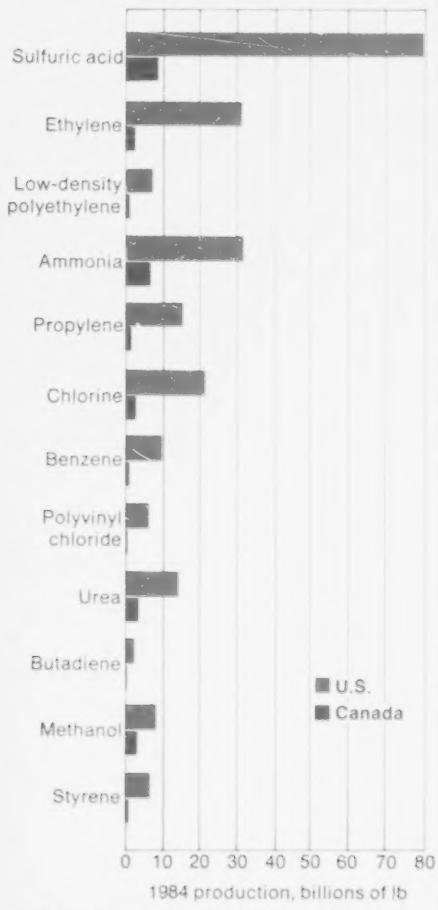
CMA also has suggested a few housekeeping provisions, such as an adequate and binding dispute settlement mechanism. It also recommends that U.S. trade officials consult with the chemical industry both before and during the negotiations.

On that score, at least, CMA's wish is already being fulfilled. Without exception, leading industry trade experts have given the trade representative's office high marks for its open-door policy. "The people over there are always ready to listen to us," says one chemical industry trade expert. Another, more cautious cynic adds, "Hearing and heeding are two different things."

The admiration is reciprocal. Top officials at the trade office have praised the chemical industry for its knowledge of trade issues. And they single out ISAC-3 as one of the most effective of all the industry sector advisory committees. To remain effective, ISAC-3 has its work cut out for it. In addition to polishing the arguments contained in CMA's set of principles, ISAC-3 no doubt will add a few of its own. For instance, the chemical industry, probably through ISAC-3, will push for exceptions lists. Such lists will contain import-sensitive products that chemical producers feel should be exempted from tariff cuts. In the past, many U.S. chemical companies have nominated products for exceptions lists. No doubt those same products will crop up again as candidates for exemption.

Meanwhile, many U.S. companies say they don't want to see chemicals "sacrificed on the altar of free

U.S. output of chemicals towers over that of Canada



Sources: U.S. International Trade Commission, U.S. Bureau of the Census, and Statistics Canada

trade," as one company official puts it. They do not want U.S. negotiators to reduce or eliminate tariffs on Canadian chemicals in exchange for Canadian concessions that will benefit another, nonchemical U.S. industry. Chemical industry trade experts with sharp memories recall that it has happened in past trade negotiations. They don't want to see it happen again.

Until now, most of the industry's efforts have been directed toward the Administration's trade officials. Industry spokesmen haven't bothered much with Congress because they haven't had to. But that will change soon. President Reagan notified the House Ways & Means Committee and the Senate Finance Committee on Dec. 10 that he intended to enter negotiations with Canada. Under a "fast-track" approach, Congress has 60 working days in which to consider the proposal. If Congress doesn't act, negotiations are automatically approved.

Trade observers think that Congress will give the green light to the trade talks, despite some Congressional apprehension about Canadian subsidies on lumber and a few other issues. It's likely, however, that the two committees will hold hearings.

That's when the chemical industry's trade experts will really roll up their sleeves. With the U.S. trade deficit at an all-time high, Congressional ears are sensitive to talk about trade balances. Chemical industry witnesses will point out that, although the U.S. industry still enjoys a positive balance of trade, its trade surplus has been dwindling rapidly. In 1980, the U.S. chemical industry had a $12.1 billion trade surplus. Last year, that surplus had shrunk to $7.7 billion.

Canada is the U.S.'s largest chemical trading partner, just as it is the U.S.'s largest partner in overall trade. The U.S. shipped $2.8 billion worth of chemicals into Canada last year and imported $3 billion in chemicals from there. That means that the U.S. had a $200 million deficit in its chemical trade with Canada. In fact, the U.S. chemical trade balance with Canada has been in the red every year except 1983 for the past eight years.

That deficit makes the prospect for free trade between the two countries an important issue for the U.S. chemical industry. Usually vocal industry spokesmen have been quiet so far—only because there has been little specific to talk about. As Congressional hearings get under way and negotiators in both countries clarify their objectives and strategies, that will change.

Many U.S. chemical companies have expressed their views about Canadian-U.S. free trade in the past. Those views haven't changed. Typically, most companies want some of their products exempted from tariff cuts. Monsanto, among others, for instance, doesn't want duty-free

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treatment given to styrene, polystyrene, and a few other products, including formaldehyde, maleic anhydride, and 2-ethyl hexanol. Other companies suggest for exemption such bulk chemicals as polyethylene, methanol, polyvinyl chloride, ethylene oxide, and ethylene glycol.

Allied-Signal also is concerned about polyethylene, but not so much as about Canada's uranium policy. Canada requires that all uranium concentrate be converted to uranium hexafluoride before it's exported. The only converter in Canada is Eldorado Nuclear Ltd., which is a subsidized national corporation.

Allied-Signal is one of only two private uranium converters in the U.S. The other is Kerr-McGee. But Canada's policy, says Allied-Signal, means that Allied-Signal cannot compete for the business of converting Canadian uranium.

On the other hand, some companies support free trade with Canada simply on principle. They range from large companies such as Dow Chemical to the relatively small ones such as Huntsman Chemical, Salt Lake City. Dow, which has a subsidiary in Canada, supports U.S.-Canada free trade as long as energy and investment policies are harmonized between the two countries and the negotiations are broad-based, rather than sectoral. Jon Huntsman, chairman and president of Huntsman Chemical, favors free trade because "protectionism only accelerates the decline of key industries." He feels that way even though his company will receive styrene from American Hoechst under a tolling agreement that makes styrene from Canada less attractive to the company.

No doubt company positions will be revised and refined as negotiations near. One factor that companies will have to pump into their equations is the impact of the recent drop in crude oil prices. How they evaluate it could help to define how they feel about the relative competitive position of the Canadian chemical industry. Several companies admit to going through the "number crunching" right now.

The drastically lower oil prices already have had an impact on Frederick Knight's thinking. Knight, a senior vice president for Borg-Warner Chemicals, opposed making tariff cuts on styrene under any Canadian-U.S. trade agreement. His reason is Canadian energy pricing policies that help to support production of styrene raw materials from tar sands in Alberta. He still opposes tariff cuts on styrene, but for a different reason. He is afraid that the U.S. government will take advantage of the recent oil price cuts and push through an oil import fee to raise deficit-reducing revenue. If that happens, Knight says, all they'd be doing is substituting a U.S. disadvantage south of the border for what used to be a Canadian advantage north of the border. □

CHEMISTRY AS A LIFE SCIENCE SYMPOSIUM-III

The third in this series of biennial symposia will be held at the
ROBESON CENTER
RUTGERS, THE STATE UNIVERSITY OF NEW JERSEY, NEWARK
FRIDAY, 21ST MARCH, 1986
Symposium to be chaired by Prof. Albert I. Meyers, Colorado State Univ.
PROGRAM

- **Welcome and Opening Remarks** 9:00 A.M.
- **"Dimensional Tolerance of Watson-Crick DNA, RNA Cross-Sections: A Synthetic Approach"** 9:15 A.M.
  Professor Nelson J. Leonard
- **Coffee Social** 10:15 A.M.
- **"Manipulation of the Arachidonic Acid Cascade"** 10:45 A.M.
  Sir John R. Vane, FRS, 1982 Nobel Laureate for Physiology or Medicine; Keynote Address
- **Lunch** 11:45 A.M.
- **"Mechanisms of Coenzyme B_{12}—Dependent Rearrangements"** 1:30 P.M.
  Professor Jack Halpern
- **Coffee Social** 2:30 P.M.
- **"Molecular Recognition: Studies of the Binding of Oligosaccharides by Monoclonal Antibodies and Lectins"** 3:00 P.M.
  Professor Raymond U. Lemieux
- **"New Synthetic Technology and Natural Products Synthesis"** 4:00 P.M.
  Professor Kyriacos C. Nicolaou
- **Wine and Cheese Social** 5:00 P.M.

The symposium is free and open to the public, but advance registration is required because of limited seating capacity (600).
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Symposium Organizing Committee: Michael Czarniecki, Michael J. Green, Stan S. Hall, Faizu Kathawala, Dennis Keith, John J. Partridge, H. Burt Renfroe.

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